

THE
AMERICAN RAILWAY
PROBLEM



AN ADDRESS BY
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IN this discussion no attempt will be made to take up any of those problems which relate to the American railway company merely as a corporation aside from its function as a transportation agency. Many questions are now actively mooted in the United States, such as those of taxation, combination, the formation of trusts, and federal incorporation, which relate to all companies. There are, however, other questions which have to do exclusively with common carriers, and of some of these I will endeavour to give a brief summary.

There are in the United States to-day about 230,000 miles of railroad right-of-way, including some 330,000 miles of tracks. This mileage is scattered over upwards of 3,000,000 square miles of area, and provides transport for the requirements of some 90,000,000 individuals. Observe how the railroads have grown and the country with them. In 1880 there were but 87,724 miles of railway. The population was about 50,000,000, or about 17 to the square mile, and the country's farms produced \$2,212,000,000 in values. The country now has a population of nearly 30 to

the square mile, and last year the value of the products of its farms was \$8,300,000,000. In thirty years there was thus an increase in railway mileage of nearly 170 per cent., in population of 80 per cent., and in the value of farm produce of approaching 300 per cent.

You have heard a good deal about railroad abuses in the United States, and yet this very period of such amazing expansion was one in which every variety of these evils flourished. Is there then, at the very outset, any escape from the impression that, whatever may have been the evils in our railroad system, that system has in actual fact contributed decisively to a commercial development unprecedented in its rapidity among the nations of the world.

It was but natural, however, that, in connection with this phenomenal development, there should have arisen many causes of irritation and friction. These evils were oftentimes quite unimportant in their inception, but as time went on they became of very serious consequence and did real harm. The purport of many of these evils, notably that involved in the freight rate rebate, was not at first clearly discerned. The railroad was a new plant, and as its growth brought so much prosperity and benefit to every one, little thought was given to the weeds which were beginning to flourish.

The feeling on the part of the public that something was wrong—intensified oftentimes by demagogues, always on the lookout for a head to hit—provoked a movement to control the railroads. This movement

started in the early eighties and, with more or less recurrent activity, has continued its influence ever since. Twice during this period violent waves of anti-railroad sentiment have swept over the country. One of these was the "Granger Movement" of 1886 and 1887, which resulted in the passage of extraordinarily radical legislation, only to have it repealed during the reaction of feeling a few years later. The other started in 1905, and has not yet entirely spent its force.

Accompanying these disturbing waves of political interference with the solving of an essentially economic problem, there has been the constant and careful study of the question by publicists, students, and railroad officers. The American people have no sympathy with any project to nationalize the railways, but they feel that there must be strong public control. It was absolutely necessary that effective measures should be taken to stop the old practices of discrimination and favouritism, of special rates and secret rebates, and of unequal treatment of shippers. Regulation was imperative, and it has served a sound public purpose.

The more profound students of the problem discerned that the philosophy of State control was based upon two facts:

1. That the State assigned to a railway the sovereign function of exercising the right of eminent domain. The railways of course had to pay heavily for every exercise of this right, but the privilege was undeniably a sovereign one.

2. That the railway was essentially monopolistic,

and that the public was absolutely dependent upon its properly performing its duties as a common carrier.

It has become an established doctrine of American public law, therefore, that the State shall have the right to protect the public against any violation on the part of the railroad of its duty as a common carrier. It has not yet become an established part of our legal framework that the State shall go further and usurp the functions of discretionary management, and, though there are many advocates of such a policy, the experience and the wisdom of our ablest men will doubtless prevent the ultimate adoption of any such heresy.

THE QUESTION OF PROCEDURE

LET us first consider the methods which the United States have adopted in attacking the railroad problem, for this question of procedure is a very important one. To understand it, one must realize the nature of our dual form of government, under which the States have exclusive jurisdiction over all questions of commerce within their own territories, while the national government has plenary power over all questions of commerce between the different states. It will be observed, therefore, that many questions of railroad control are within the power of individual states, while many others are subject to the action of the national government.

The effort to right the wrongs of railroads and to protect the public against improper transactions has taken three general forms:

1. The passage of laws directly by the National

Congress and by the State Legislatures. We in America have great faith—too great faith, many think—in legislation. You may gather some idea of the extent of this faith from the statement that in the last Session of Congress there were introduced 28,440 bills, and in the 1909 Session of 39 State Legislatures, 45,330 bills, or a total of 73,770 for the country in two years. During that period Congress enacted 326 bills (exclusive of pension bills) and the 39 State Legislatures 12,508. Thus a total of 12,834 bills became laws. A great many of these bills related to railroads, some of them arbitrarily reducing rates of freight or passenger fares. The Courts have proved a bulwark against a large quantity of this ill-advised legislation, and, in addition, a good share of it has proved futile because of sheer impracticability.

The recognition that large legislative bodies could not deal in detail with such intricate and delicate problems as were involved in railroad control, has led to the adoption of the other two methods of procedure:

2. The creation of State railroad or public service commissions to exercise on behalf of the State legislatures their right of control; and,

3. The appointment of an Inter-state Commerce Commission to exercise the functions of the national legislature in dealing with these problems.

THE STATE COMMISSIONS

THE most successful of our State railroad commissions, in the opinion of such intelligent students of the rail-

road problem as your own Mr. W. M. Acworth, is that of the State of Massachusetts. This Commission has nominally little power, except to secure publicity. If a trade or a locality considers itself badly treated, the Massachusetts Commission hears the complaint, listens to the answers of the railroad company, and then expresses its own opinion. Throughout the thirty years' history of the Commission, its decisions have almost invariably been accepted as just by both sides, and the results of the Commission's work have been most salutary.

Because, in so many cases, the very creation of these state commissions was the result purely of political agitation, their members have felt that they must show good reason for their existence by doing something spectacularly radical. Curiously enough, public sentiment has generally prevented the appointment to these commissions of men who had had practical experience as railroad officers. In brief, the heedless creation and appointment of these commissions has oftentimes been an injury rather than a benefit to the public, and as there is no organic relationship between the commissions of the different states, there has grown up a complicated set of rulings, often mutually contradictory, as between two neighbouring States, both penetrated by the lines of the same railroad company. A great improvement, and one that promises steadily increasing public benefit, is the plan, now a few years old, whereby the members of the different state commissions meet in convention once

a year and, jointly or through their committees, discuss various questions which are before them in an effort to arrive, if possible, at uniform methods of procedure. There has also been a noticeable improvement in the *personnel* of the state commissions in recent years, and their members are, in general, earnestly striving to work out their very difficult problem to the benefit of every interest concerned.

THE INTER-STATE COMMERCE COMMISSION

THE Inter-state Commerce Commission is a very peculiar body, possessing as it does functions which are, at the same time, inquisitorial, administrative, and judicial. The absurdity of combining these relationships has been recognized both by railroad officers and statesmen. To separate some of these functions, there has just been introduced in Congress, with the sanction of President Taft, a bill providing for the transfer of many of the judicial functions of the Commission to a so-called Court of Commerce. This Court, it is proposed, shall have original jurisdiction over all cases involving orders of the Inter-state Commerce Commission. It will protect litigants from the legal delays, which are often to be met with in present procedure, and will tend to build up a structure of railroad law in the United States which will be a protection both to the railroad companies and to the public.

The Chairman of the Committee on Inter-state Commerce of the House of Representatives has also

introduced an entirely separate bill providing for the creation of an executive "Bureau of Transportation," where a shipper may file a complaint. If the head of the Bureau finds that there is justice in the complaint, he will report the facts to the Attorney-General of the United States, who may file a petition with the Interstate Commerce Commission and prosecute the case at the expense of the Government. The shipper may, if he prefers, still file his complaint direct with the Commission and prosecute it at his own expense, as the present law provides. You will note, therefore, a tendency to divide the functions now exercised by the Commission into several parts, and there is every reason to believe that in the near future a plan will be worked out whereby the procedure in settling the rights of the public and the railroads will be made much more expeditious and clear, and, as a consequence, more equitable.

THE PROBLEM OF MANAGEMENT

THE question of procedure, however, is not the problem itself. The railroad problem proper in America to-day naturally divides itself into many distinct phases, three of which are acute at this moment. The first of these is a problem of management, that is of handling the traffic for the lowest cost, or, in other words, of keeping as safe a margin as possible between the revenues of the companies and their expenditures.

The total operating earnings of the railroad com-

panies of the United States for the year ending 30th June 1908, were \$2,393,805,989. The expenses were \$1,669,547,876, leaving net earnings of \$724,258,000. From these net earnings there had to be deducted taxes amounting to \$78,673,794. There has been a constant increase of taxation in recent years. The taxes per mile of American railroad corporations for the year ending 30th June 1898, were \$178.64, while for 30th June 1908, they had increased to \$255.70, an increase of 43.1 per cent. The ratio of tax to net earnings had increased from 10.2 per cent. in 1898 to 11.4 per cent. in 1908. Note on the other hand how the revenues per unit of traffic have steadily declined. The average earnings per ton per mile of the railroads of the United States were in 1888, 1.001 cents, while in 1908, they had decreased to 7.54 cents.

The fact that the railroad companies were able to maintain and in many cases increase dividends, as well as meet their constantly growing expenditures, against this steady decline in rates, has been due to an extraordinary development of efficiency in operations, which has made possible a steady decline in ton-mile costs.

Through the policy of the companies in appropriating large sums out of earnings for improvements, it has been possible to reduce grades, eliminate curves, and otherwise improve the roadbed. With the improvement of track there has gone a steady development of the train as a machine for moving traffic. Statistics will show that, since 1870, while the average number of miles per unit of traffic, run by freight trains in the United

States, has been actually decreasing, the average number of tons carried one mile has been more than trebled. This has been due to great increases in the tractive power of locomotives and in the capacity of separate freight cars.

The costs of commodities have caused great and steadily increasing additions to the expenses of the railroads, and, at the same time, there has been a steady increase in the rate of wages. Our railroads employ about 1,700,000 men and each year pay out in wages approximately \$1,400,000,000, about \$900 per man. In 1906 practically all the railway companies increased the wages of their men about 10 per cent.

The Pennsylvania, the largest of our railroad corporations, employing approximately 200,000 men, had previously increased the wages of its men by 10 per cent. in 1902. This Company to-day pays its employees at a rate about 22 per cent. higher than it did 10 years ago. The greater portion of our railroad employees are combined into various unions. Some of these unions are very strong and are managed by crafty and, in some cases, unscrupulous, or at any rate, demagogic leaders. For a long time these unions dealt with railroad companies individually on behalf of the employees of the particular corporations. There has recently been a tendency, however, among the different unions to combine and present their demands jointly to an entire group of railroads, with the implied threat at all times that, unless their demands are granted, the employees of all the railroads concerned will go out on strike.

This, of course, would at any time be a most serious blow to the daily life of the country, and every influence is consequently brought to bear to prevent such a contingency from becoming a fact.

THE DEMANDS FOR HIGHER WAGES

THE railroad unions are to-day presenting demands for increased wages to different companies, particularly in the section east of the Mississippi River. Within the next few months you will probably find that there will be presented jointly to the eastern railroads a demand for higher wages. This will be accompanied by various absurd rumours in the newspapers, of a possible strike and a fight to a finish. At a critical point in the negotiations a representative of the Inter-state Commerce Commission will probably be called in to mediate. An effort will undoubtedly be made to have the decision postponed, in the hope that the present tendency towards a higher cost of living may be checked. If the final decision can be postponed, a large increase will probably not be allowed. If, however, a decision is forced before the year's crops begin to mature, there is likely to be a general increase of 5 or 10 per cent. in our railway wages.

It must be obvious to any student, that these frequent increases in wages cannot be made indefinitely. The tendency is not only to compel increases during times of prosperity, but to prevent decreases in times of depression. Neither the railroad nor the public can work along properly with threats of strikes continually

before them. So important is it to secure a permanent decision upon this question, that far-seeing railroad managers of America to-day are giving most earnest thought to the working out of some system of profit-sharing, whereby employees may gain some share of the increased prosperity, and at the same time share in the adversity of their companies. Before a great while you will find that our more progressive companies will have a profit-sharing scheme, a system of old-age pensions and a plan of employers' liability. This will make for stability and safety of employment and will add to the permanent efficiency of the companies.

Right here let me interject the observation that the railroads themselves are making a most effective contribution towards reducing the high cost of commodities. Although there has been an enormous increase in the output of agricultural lands in recent years, the intensive development of the country has not proceeded apace. Probably no country in the world excels the United States in natural fertility of soil, or has a more favourable general climate ; but with our careless and uninformed methods of seed selection, fertilization, and cultivation, the annual wheat yield of our farms is less than fourteen bushels per acre, as compared with thirty-two in England, twenty-eight in Germany, thirty-four in Holland, and twenty in France. Of oats, the United States produces something less than twenty-three bushels per acre, while England produces forty-two, Germany forty-six, and the Netherlands fifty-three.

Thus, with us, the pressure upon agricultural output has become greater than the supply. The railroads, having perceived the meaning of this condition, are to-day proving most powerful factors in the inculcation of intelligent farming methods. Mr. James J. Hill is a veritable apostle crying in the wilderness on this subject. The New York Central Railroad Company has established five experimental farms for the purpose of demonstrating to farmers how they can produce forty bushels to the acre. The Long Island Railroad Company and many others have also done pioneer work in this direction. So that the railroad is not only opening up land and making it accessible to commerce, but it is also demonstrating to the farmers, through co-operation with agricultural colleges, how the land may be made productive. This missionary work, when fully applied to our great area of agricultural land, will inevitably produce results of widespread import.

THE PROBLEM OF TRAFFIC

So much, then, for the problem of management. The limit has about been reached in reducing expenditure through increasing the efficiency of the railroad machine. Unless there is some revolutionary discovery, the size and power of locomotives cannot be further enlarged. The limit has about been reached, also, in the capacity of freight cars. So it is not likely that there can be further decreases of importance in the cost of handling the ton-mile. Of course, some propose increasing the gauge of the tracks, and others

foresee economies through electric traction. But, before either of those influences could affect the situation, there would of necessity be an added outlay of capital, the enormous quantity of which it is almost futile to attempt to estimate.

So able a railroad economist as President Brown of the New York Central Railroad, recently stated that there was no possibility of much further reduction in the cost of conducting transportation, and that any further material change in conditions, such as increased taxation, demands for higher wages, greater cost of material, and the like, would undoubtedly necessitate further additions to freight rates.

Consequently, we are brought face to face with the second of our great problems, viz.: a question of traffic, that is, obtaining a price for the company's service which will pay expenses and return a fair rate of interest upon the investment.

Here we enter one of the most complicated and at the same time one of the most fascinating domains of railroad work. Railroad rates in America have until the last few years been exceedingly elastic. It can be fairly said that in England, the country built up the railroads, but that in the United States, the railroads built up the country. Our amazing prosperity has been due, in large measure, to the railroads so adapting their rates and their service as to promote at every point the interests of commerce. The phrase, "What the traffic will bear," has been crucified for many transgressions, but its real result has been to annihil-

ate distance, to decentralize markets and population, and to develop prosperity. Our railroad rates, consequently, constitute an exceedingly delicate structure, born of commercial conditions, made effective by a body of carefully trained and thoroughly competent traffic officers, who have given their lives to a study of their difficult tasks.

In the light of the palpably increasing costs of railroad operation, there is a large body of intelligent public sentiment in the country, which believes that the railroads would now be justified in making a general increase in rates. It is understood that even the chairman of the Inter-state Commission himself agrees to the justice of this proposition.

But even though this may be the sentiment on the general economic question, we suffer rather acutely in America from what Mr. Acworth calls "the inconvenience of dealing with economic problems by legal machinery," or, in other words, too much politics. Thus, while economic sentiment, if I may so describe it, sanctions an increase in freight rates, there is a large and powerful body of political opinion which advocates such severe restrictions upon the right of the railroads to establish their own rates, as to amount, in effect, to a virtual prohibition of a reasonable readjustment of rates to commercial conditions. Up to the present, the general theory underlying the work of the Inter-state Commerce Commission has been that the Commission should prevent rebates, secure publicity for rates and accounts, and, upon complaint

of an injured party, revise and prescribe rates and practices.

THE EFFORT TO COMPEL COMPETITION

HERETOFORE, we have sought to compel competition between railroads, yet now, while not abandoning the theory of forced competition, the tendency of our legislation is absolutely to destroy whatever competition in rates there still remains. To particularize: The idea controlling our original legislation was to force competition by prohibiting the railroads from making any agreements or arrangements among themselves relating to rates or practices. Being legally unable to make agreements, the companies were forced to make purchases of stock in each other's properties, in other words, to develop what we call a "community of interest," to maintain unity and harmony of management. The companies, acting under authority granted by the various States, acquired interests in various roads, some of these interests being in extensions, some of them in feeders, while others are in lines actually parallel and serving the same territory. Among the more noteworthy and, I may add, beneficial of these purchases was the acquisition by the Union Pacific Railroad of a large interest in the Southern Pacific Company. Actions are now pending in the courts to dissolve some of the combinations which have taken place, and the President has recently recommended that further legislation be enacted to prevent such purchases in the future. Thus we have

here one class of governmental activity seeking to force competition.

Let us now examine those contradictory forces, the effect of which is to stifle competition. All railway rates and practices to-day are by law given complete publicity, and cannot be changed without notice, and that means, of course, without the knowledge of all competitors. Any attempt to secure business through giving better rates or service, being known, is at once met by a rival road. If a company under such circumstances files a new schedule of rates, or of more favorable usages, instantly the rival does the same thing, putting itself precisely on the same basis and thus destroying all competitive effort. We have thus eliminated competition, substituting therefor Government regulation and Government control.

PROPOSED RATE REGULATION

HAVING secured this publicity of rates and placed the Government in a position to correct unreasonable rates after complaint is made, the present law permits the companies to make rates freely, stipulating only that the rates shall be duly filed with the Commission. The Commission may not investigate an increase of rates till after the rate becomes effective. It is now proposed by the President to empower the Commission to postpone the effective date of an increase in rates until an inquiry into its reasonableness may be made. Those who favour this amendment to our practices argue that the fact that a rate has been in effect should

be regarded as *prima facie* evidence of its reasonableness, and that a railroad should not be permitted to change it without justifying its action before a competent tribunal.

This argument, of course, entirely overlooks that most valuable feature of our present railway rate system, its flexibility and adaptability to changing industrial and commercial conditions. The proposed change embodies the principle and the practice at present prevailing in England, the result of which, I have been informed, is effectually to prevent frequent and temporary decreases in rates to meet special conditions. Railway men know that, if a rate cannot be increased without extreme difficulty, every inducement to reduce rates under special conditions will be taken away.

Heretofore the assumption has been that railroads would establish reasonable rates only, and that the right of the carrier to establish its rate should not be disturbed until it had been clearly shown that injustice has been done. The proposed law would empower the Commission, upon its own initiative, to examine and suspend the operation of any rate or schedule which might be filed with it. Now, as nearly 200,000 tariffs are annually filed with the Commission, obviously all of them cannot be examined. Railroad managers claim that the suspension of even a limited number would destroy the relative adjustment of rates, and create both confusion and discrimination against individual shippers and communities.

This whole proposition was before the last Congress in the form of a bill introduced by Senator Fulton of Oregon, but it was effectually disposed of by a very able report submitted by the Senate Committee on Interstate Commerce.

A GENERAL REVISING POWER

BUT the would-be reformers of our railway laws do not stop here. A bill has been prepared under the direction of the President and introduced in Congress which, while not making it the duty of the Inter-state Commerce Commission to prescribe all rates, actually puts it in the power of that body to supervise and dictate the whole rate-making system of the railroads of the country, a power which, if much exercised, would be extremely harassing to the railroads. It is not to be assumed that such a power would be exercised arbitrarily with the purpose of causing trouble, but it would be liable at any time to be so used, and would be a continuous menace.

The bill further provides that the Commission at any time, on its own initiative, may order a hearing, and if it decides that any rates, charges, classifications, regulations or practices whatsoever, affecting rates are improper or unreasonable, it may prescribe the rates, regulations, or practices which shall be observed in lieu of those declared to be unlawful. This would give it power to overhaul and upset rates and regulations whenever a majority of its members thought there might be occasion for intervention.

Considering what a network our system of rates and classifications is, and how a change at one point may compel new adjustments at other points, it is obvious that the exercise or even the existence of such a power would have a disturbing effect upon railroad calculations and management. Railroad managers even now find it necessary, on account of shifting conditions of traffic, to be almost constantly readjusting schedules of rates; they can no more be fixed and permanent than the market prices of commodities. Experienced men know that it requires experts trained in railroad traffic, and fully acquainted with the conditions affecting it and affected by it, to adjust rates to the best advantage of shippers and the public, as well as of the carrying companies themselves. This work cannot possibly be performed by an official body, inexperienced in the actual business, and burdened with multifarious other duties. Even so radical an authority as Mr. Roosevelt, when President, expressed the opinion that "it would be undesirable if not impracticable finally to clothe the commission with general authority to fix railway rates." Mr. S. C. T. Dodd, the famous Solicitor for the Standard Oil Company, once said to me, "Statutes may temporarily interfere with commerce, but they can never interfere with the inexorable operation of economic law."

It does not seem unwarranted, therefore, to conclude that, by just so much as some of these propositions are crude and uneconomic, by just so much is it

unlikely that they will ever become or remain law. The people of our country have ingrained within them a large quantity of rugged Anglo-Saxon common sense, and in the long run their decisions are apt to be eminently sane and practical.

It must, however, be apparent to you that the actual effect of these proposals is toward preventing, or, at least, toward giving the state the power to prevent, increases in rates. We come face to face then with the problem involved in Mr. Acworth's alternative: "If one half of the rates are to be kept down by economic and the other half by legislative compulsion," where is the dividend to emerge?

THE PROBLEM OF FINANCE

HERE then is our problem of finance, namely, that of so operating the railroad at present, and of offering such promise for the future, as to obtain the capital with which to develop the property and provide for its expansion.

Our railroad companies as a rule have charters granted by the states, and the states prescribe the methods of capitalization. It is now proposed by the President that, whatever may be the nature of these state charters, the railroads shall be able to issue securities only after obtaining the approval of the Inter-state Commerce Commission. On this proposition, one of our great constitutional lawyers, Senator Spooner, recently expressed this opinion: "I have not yet been able to satisfy myself that where one

government creates a stock corporation, another government shall regulate the amount of its capital stock and its bonded indebtedness."

Much of the proposal to give the Inter-state Commission power over security issues is based upon the theory that even if the railroads have not been mismanaged as railroads, they have been exploited as financial undertakings, and that this has been productive of watered stock and over-capitalization. From this proceeds the further fallacious notion that railroad rates are based upon capitalization, and that the corporations are charging exorbitant rates in order to pay dividends on their watered stock.

Any one familiar with the making of rates knows that capitalization has but little to do with it. If plenary rate-making powers are to be given to the commission, and the commission at the same time shall receive authority to prescribe the terms upon which railroad corporations shall be permitted to borrow money, it is clear that stockholders and directors will retain a very limited control over the management of their profits. This extreme eventuality is not likely to take place, but to show how far the idea of interfering with railroad management has penetrated the minds of people, permit me to call your attention to this highly paternalistic quotation from the latest annual report of the Public Service Commission, Second District, of the State of New York:

"Any system of law which permits uninstructed investors to place their money in stocks of public

service corporations which either ought not to, or cannot yield, any return and which, in fact, are non-productive, is distinctly injurious to the non-investing as well as the investing public."

THE REGULATION OF SECURITY ISSUES

TWO distinct propositions are offered by President Taft to solve this problem of capitalization. First, that the Commission shall have supervision over the question as to whether or not securities shall be issued, and for what amounts, and, secondly, that, without the permit of the Commission, no stocks or bonds shall be issued at less than par. The fundamental objection made to this second proposal was stated in a sentence by the late E. H. Harriman, who, when testifying in 1907 before the Inter-state Commerce Commission, said, "Too much importance is attached to what is called over-capitalization. The capitalization of any railroad or any corporation must be taken upon the basis of the charge for interest which it assumes." So much confusion has indeed been caused by the assigning of a par value to issue of shares, that eminent authorities have suggested the wisdom of having no par values at all, but merely allowing each share to represent its fractional proportion of the assets of the corporation.

There is no doubt that every curb should be placed upon the over-issue of capital securities, but competent financiers urge that the proposal now made would not secure the desired result. The issuance of stock beyond

the face amount of the actual investment has, in railroad building, always represented the excess of faith on the part of the builder in the success of his project. It has been the lure which has drawn him into always uncertain and often desperate undertakings.

Railroad construction in our new western country is necessarily hazardous, owing to the danger of destruction from wash-outs and the like. Railroad builders will not undertake to develop such sections by laying tracks and opening new roads unless they see their way clear to make a profit. If the possibility of that hoped-for profit be taken away, the independent railroad builder will abandon the field, and railroad extensions into vast portions of our territory which are now unserved will await the initiative of the larger and more prosperous lines. That great territory west of the Mississippi and south of the Mason and Dixon's line would be most seriously affected, but populous New England, on the other hand, scarcely at all. It would admirably serve the interests of our larger railroad systems if Government limitation of capitalization should make it impossible for the independent railroad builder to invade these promising preserves, and thus leave their development to the convenience of existing lines.

In England, I am advised, the requirement that stocks and shares should not be issued at a discount has actually been relaxed by the last Companies Act, and if a country so well settled as England finds a provision of this kind unwise, a country where enter-

prise is essentially more speculative can hardly be wise in adopting the contrary policy.

THE VALUATION PROPOSAL

SO obsessed have some of our people become with the idea that our railroads are paying dividends and collecting rates upon watered stock, that it has been urged that a fair basis of capitalization can only be reached when a complete physical valuation of our railroad properties is made. The Inter-state Commerce Commission has for a great many years very actively supported this scheme. The President has not yet endorsed it. If a basis of valuation could be agreed upon, the plan might be worked out. But it is quite certain that whatever the basis—cost of reproduction, earning power, or what not—the value would be constantly changing and no two persons, however expert, would agree upon a result. A fair valuation of the railways of the United States to-day would probably disclose the possession by the companies of assets very much in excess of their capitalization, and, but for possibly misleading inferences which would be drawn from such necessarily unscientific methods, the railroad managers would have no objection to the scheme being carried out.

There is another factor involved in issuing securities the effect of which cannot be minimized, and that is, that neither the railroad company nor the State can control the price at which securities can be issued, if they are to be issued at all. Corporations must go to

the money markets of the world for their funds, and these markets make their own terms, regardless of statutes or political movements.

Intelligent economists expect that the next few years will witness an era of amazing enterprise in all parts of the world, consequent upon the development of the steam engine, electric power, the telephone and other modern labour-saving devices, which are all now uniting with a great deluge of gold to quicken the energies of mankind into unprecedented activity. This, of course, will produce a great pressure upon capital, and, in this effort to obtain capital, the United States will be forced to offer the best terms it can. In the early days the railroads of America were developed largely by foreign capital. The time has now come when, with the tremendous demand for capital for use in industrial development, we must again look largely to Europe for the funds with which to make the necessary extensions of our present railroad lines. To get these funds our terms must be inviting. Obviously, then, to say that securities to be issued by the railroads shall only be put out at par, is another way of saying that companies, which are unable to pay a sufficient rate of dividend to make their issues worth par in the markets of the world, can not issue securities at all.

REGULATING THE TERMS OF ISSUES

BUT here the retort is made that, under the proposal of President Taft, the railroads will be able to issue

stocks or bonds at less than par if the terms of the issue shall receive the approval of the Inter-state Commerce Commission. Competent railroad financiers urge that this proviso is absolutely impracticable. For example, in 1908 the Pennsylvania Railroad Company made an issue of \$40,000,000 in bonds at 96. The money market and business conditions had been very unpromising. The managers of the railroad had been in grave doubt as to whether the time had arrived for them to place this issue. It was finally arranged, however, that the great house of Rothschilds should unite with the firm of Kuhn, Loeb and Company in New York in under-writing the securities. The success which attended the issue itself was generally considered to be due to the fact that such strong support had been obtained. But this strong sponsorship in Europe was only secured after the most delicate negotiations, and was not finally arranged until the very eve of the announcement itself. Had it been necessary for the financiers of the company not only to have conducted these delicate negotiations with foreign bankers, but also to have submitted the whole question to the Inter-state Commerce Commission, it is doubtful if the issue could have been made at that time.

Railroad managers and lawyers will undoubtedly be able to demonstrate to legislatures and courts the impracticability of these suggestions. Even now there are rifts in the clouds. The highest Court of the State of New York has just decided in a case involving the right of the Delaware and Hudson Railroad Company to

issue certain bonds, that the State Commission cannot interfere with the terms of security issues. The Delaware and Hudson Company had issued short time notes at high interest to enable it to pay for the securities of certain smaller railroad companies. Application was made to issue bonds to take up the notes. In refusing its assent to the issue of these bonds, the New York Commission held that while the purchases made by the Company were perfectly legal, nevertheless the purchase of these subsidiary securities was "unfortunate" and the price paid was too high, and that, consequently, bonds should not be issued to refund the purchase. In passing upon an appeal made by the Company, the New York Court of Appeals held, in effect, that this was for the directors and stockholders of the Company to decide. The law was not designed, says the Court, "to make the Commissioners the financial managers of the corporation," and did not empower them "to substitute their judgment for that of the board of directors and stockholders of the corporation as to the wisdom of the transaction," but only to make them "the guardians of the public by enabling them to prevent the issue of stock and bonds for other than the statutory purposes."

This appears to draw a clear line between the authority vested in the Public Service Commission and the discretion which belongs to those responsible under the law for the management of the corporation. This is undoubtedly a principle which eventually will prevail. A railroad should only be permitted to issue

securities for proper railroad purposes, but the State should not undertake to regulate the terms of issues. The step between this and actually guaranteeing the issue is too narrow.

These are but a few of our railroad questions. The general principles behind much of the radicalism which I have explained, rests upon the doctrine that the government should control and, to a large extent, operate railroads without going to the expensive risk of buying and owning them. To state this doctrine is but to disclose its futility.

There are many other allied questions which time hardly permits presenting. The American railroads are sound. Their officers are earnest men, intelligently striving to do their duty. The results of their work speak for themselves. In spite of all difficulties, they have gone ahead building up the properties, rendering an efficient service to the public and faithfully discharging their trusteeship for the stockholders. I know of no class of Americans who are more competent or who more thoroughly deserve the confidence of the public than those who are in charge of the management of our railroads.

The statesmen who have the power further to regulate railways are in the main also earnestly striving to protect all interests. Demagogic treatment of the subject is becoming unpopular. President Taft, even though he has recommended to Congress the passage



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of drastic legislation, has shown a commendable disposition to seek expert advice from our great railroad leaders. A problem having so vitally to do with the welfare of a great nation is not easily solved. But there is reason, founded upon a realization of that sense of intelligent fair play which has in the end always prevailed with the American people, to believe that these difficult and complicated questions will, in the course of a reasonable time, be settled upon a basis which will insure the continued prosperity of the railroads and the uninterrupted development of the country.

